INDEX

Page

Statement of the respondent 1

Reasons for denying the writ 2

Class protected—reasonable investor trust 2

Class protected and class obligated 4

A substantial departure from accepted course of judicial proceedings 7

Federal Court decision in conflict with controlling state law 8

Conclusion 9

Cases Cited

Brown v. Bullock, 194 F. Supp. 207 (S. D. N. Y., 1961), aff'd 294 F. 2d 415 (2nd Cir., 1961) 5

City National Bank of Fort Smith, Arkansas v. Vanderboom, 422 F. 2d 221 (8th Cir., 1970) 2

City National Bank v. Vanderboom et al., 290 F. Supp. 592 (W. D. Ark. 1968) 2

Heit v. Weitzer, 402 F. 2d 909 (2nd Cir., 1968), cert. denied, 395 U. S. 903 (1969) 2, 3

Kohler v. Kohler Co., 319 F. 2d 634 (7th Cir., 1963) .. 4

Mothner v. Ozark Real Estate Co., 300 F. 2d 617, 621 (8th Cir., 1962) 9

Myzel v. Fields, 386 F. 2d 718 (8th Cir., 1967), cert. denied, 390 U. S. 951 (1968) 3-4

Securities and Exchange Commission v. Texas Gulf Sulphur Co., 401 F. 2d 833 (2nd Cir., 1968), cert. denied, 394 U. S. 376 (1969) 2, 3

Shappirio v. Goldberg, 192 U. S. 232 (1904) 4

Skelly Oil Co. v. Phillips Petroleum Co., 339 U. S. 667, 674 (1950) 9

Statute Cited

Securities and Exchange Act of 1934:

Section 10(b) 3, 4, 6

Rule 10b(5) 3, 4, 5, 6

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1969

No. .....

THE CITY NATIONAL BANK OF FORT SMITH, ARKANSAS,
a National Banking Association,
Respondent,

vs.

ILO VANDERBOOM (Appellant in No. 19,550), DeHAAN LIVESTOCK & GRAIN FARMS, INC., a South Dakota Corporation, ANDY D. DeHAAN, KENNETH J. DeHAAN and LYLE R. DeHAAN (Appellants in No. 19,551), H. T. RINGLING (Appellant in No. 19,552), JAMES NACHTIGAL (Appellant in No. 19,553), and ROBERT CARTER (Appellant in No. 19,554),
Petitioners.

BRIEF AND ARGUMENT

Of Respondent in Opposition to Petition for Writ of Certiorari

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STATEMENT OF THE RESPONDENT

Respondent must respectfully but firmly take exception to petitioners' characterization of the facts which purportedly give rise to their justification in seeking cer-

tiorari and review of the lower Court's decision in this case. It is very clear from a reading of both lower Courts' decisions, **City National Bank v. Vanderboom et al.**, 290 F. Supp. 592 (W. D. Ark. 1968) and **City National Bank of Fort Smith, Arkansas v. Vanderboom**, 422 F. 2d 221 (8th Cir., 1970), that petitioners have not included the pertinent facts upon which these decisions are based. The basic, operative and material facts recited in both lower Court decisions were uncontroverted. Those which might have been controverted were found not material to the issues, and when applied to the applicable law, resulted in decisions for respondent in both lower Courts.

No useful purpose could be served by detailing the undisputed material facts upon which the decisions were based, but a review of the decisions found at Pages A-1 to 19, and A-21 to 61 of the petition will easily identify the proper and significant facts to be considered.

REASONS FOR DENYING THE WRIT

Class Protected—Reasonable Investor Test

Petitioners have suggested that the opinion of the Court of Appeals departed from the rulings of other circuits in establishing an objective "reasonable investor test", in conflict with **Heit v. Weitzer**, 402 F. 2d 909 (2nd Cir., 1968), cert. denied, 395 U. S. 903 (1969), and **Securities and Exchange Commission v. Texas Gulf Sulphur Co.**, 401 F. 2d 833 (2nd Cir., 1968), cert. denied, 394 U. S. 376 (1969).

This contention could only be based upon either a complete lack of understanding of the Appeals Court's decision, or an intentional disregard of the language of that opinion. The Court did not establish a new test for

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determining the class of persons protected by Section 10(b) of the Securities and Exchange Act of 1934 and Rule 10b-5 promulgated thereunder. The question considered was whether or not petitioners, based upon their purchase of stock in the corporation which they established, Investors Thrift Corporation, were a part of a class to be protected by the statute and rule.

The Court of Appeals determined from uncontroverted facts that petitioners did not purchase Investors Thrift Corporation stock from the Respondent, but purchased it from their own corporation which they had earlier organized and in doing so, relied upon their own agent, Markham. One of the petitioners, Vanderboom, even traveled to Arkansas to visit and examine the books of the two companies. Investors Thrift Corporation, **not petitioners**, had an option to purchase the stock in Peoples Loan and Investment Company (PL&I). Other pertinent facts were considered and determined by the Court of Appeals before concluding that the petitioners could not have relied upon any representations by the respondent Bank, and that the Bank did not owe a duty of full disclosure to them under the undisputed facts, which showed that Markham, petitioners' agent and president of Investors Thrift Corporation, had access to all financial data for more than a month before the option was exercised and four months before the option need be exercised.

Thus, the Court of Appeals relied upon and followed both **Texas Gulf Sulphur** and **Heit**, *supra*, in adopting the "reasonable investor" standard and correctly applied the test to the facts of the instant case concluding, properly, that its application to petitioners did not afford coverage. Petitioners do not disagree with the lower Court's finding that petitioners had the means of knowledge at hand and furnished to their agent. **Myzel v.**

Fields, 386 F. 2d 718 (8th Cir., 1967), cert. denied, 390 U. S. 951 (1968). **Kohler v. Kohler Co.**, 319 F. 2d 634 (7th Cir., 1963). **Shappirio v. Goldberg**, 192 U. S. 232 (1904).

If any conflict exists between circuits, it is only with respect to the questions of negligence and/or scienter, clearly a secondary matter in the instant case as reflected by the operative facts.

Class Protected and Class Obligated

The Court of Appeals in this case correctly determined that petitioners do not satisfy the "purchaser-seller" standing requirements of Section 10 (b) and Rule 10 b-5. The lower Court went further to hold that the proper course of action for petitioners would be to raise any 10 b-5 claim which they might have by bringing a derivative suit on behalf of Investors Thrift Corporation.

Petitioners challenge the Court of Appeals' decision and attempt to characterize its decisions as limiting the class of persons protected to direct purchasers and sellers, and thus relieving third parties which commit acts allegedly amounting to common law fraud or a violation of Rule 10 b-5. This argument has been projected either upon a lack of understanding of the Court of Appeals' decision or a deliberate attempt to misconstrue its meaning.

Even a cursory reading of the Court of Appeals decision reflects an acknowledgment of the mitigating doctrines which give standing to certain plaintiffs who are not technically purchasers or sellers of securities (See page A-11 to 12 of the petition).

It is abundantly clear that the lower Court determined that petitioners did not reach the requisite "standing to sue" requirements based upon the controlling facts in the

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instant case. Not overlooked by the Court of Appeals were such significant factors as petitioners' claim in the lower Court that Investors Thrift Corporation, the actual purchaser of the securities, was never an operating company and its corporate structure was a mere conduit which was convenient for petitioners to use in making this purchase. Petitioners here have not even attempted to dispute the finding of the Court of Appeals that Investors Thrift Corporation was a bona fide corporate entity and not merely a conduit. The Court's attention is invited to Page 21 of the petition where petitioners candidly admit that Investors Thrift Corporation did not borrow funds from the Bank and "did not receive nor act upon the misrepresentations and concealment of material facts by the Bank officials. . . ."

Respondent certainly would agree that the strict privity requirements by purchaser and seller are no longer a present requisite to recovery under Rule 10 b-5, but urge that the numerous cases cited by the Court of Appeals and the petitioners establish that each case must turn upon its own set of facts.

Petitioners have cited the case of **Brown v. Bullock**, 194 F. Supp. 207 (S. D. N. Y., 1961), aff'd without discussion of this point, 294 F. 2d 415 (2nd Cir., 1961), for the purpose of alleging that the Second Circuit has relaxed the privity requirements. No issue is taken with that argument even though the case is not a securities case, per se. The significance of that decision, however, is not the fact that privity is not an ultimate or an operative fact, but rather an evidentiary fact to be considered in conjunction with other material facts in determining the relationship, if there is one, between the plaintiff and the defendant and the exact nature of particular acts and transactions which may involve a duty created by the statute. As so aptly pointed out in the decision of the

Court of Appeals, the privity requirement was not met, and the operative facts did not as a matter of law place the petitioners within that group protected by the statutes or the rule.

Respondent respectfully submits that there is no conflict in either of the lower Courts' decisions and the cases cited by petitioners. Rather, each case must turn on the factual situation. The speculative questions raised in petitioners' brief and the projection of theories to absurd conclusions are unwarranted if they are intended to be based upon the findings and holdings of the Court of Appeals. Certainly, that Court's decision cannot be treated as a nullity. As in most cases, this one was decided upon its own peculiar set of material facts and does not present a conflict between circuits nor a departure from other Courts' holdings. Here is simply a determination by the Court applying existing applicable law to undisputed and uncontroverted material facts.

The Court of Appeals' suggestion that the shareholders of Investors Thrift Corporation could have brought a derivative action filed on behalf of the allegedly injured purchaser was proper, and the reasons for not bringing such a suit are known only to petitioners who elected not to bring such a suit.

It seems fair to conclude after considering the facts stated by both lower Courts, the petitioners made this election because if anyone made misrepresentations to them—if anyone perpetrated fraud upon them—it was their agent, Markham, and his corporation, Investors Thrift, and not the respondent Bank.

Petitioners, in an obvious—if not blatant—attempt to catch the eye of this Court have overstressed Section 10 (b) of the Securities Act and Rule 10 b-5 of the Securities

and Exchange Commission. The record, and both lower Courts' opinions demonstrate, as will be shown next, that much more was involved in the conclusions of the lower Courts, and their ultimate decision that while petitioners may have been lured by Markham into investment that, because of his mismanagement, turned out badly, they cannot now place the responsibility on the respondent Bank, which, after all, made loans in substantial amounts to petitioners, and entirely in good faith.

A Substantial Departure From Accepted Course of Judicial Proceedings

The matters presented under this caption of the petition essentially complained that petitioners were denied a trial by jury. Petitioners do not urge that summary judgment is not an accepted course of judicial proceeding, but rather complain that there are material and disputed facts. The only substantive contention that material facts are in dispute is based upon the lengthy, involved and wholly irrelevant question propounded in their opening paragraph of this part of the petition. In other places of this response it has been noted that all the material facts were undisputed, and that petitioners did not fall within the class of those persons protected by the applicable statute and/or rule.

Particularly significant in this argument is petitioners' admission at page 25, "The issue of reasonable investigation by the petitioners of the representations made by the Bank was not considered by the petitioners, nor their counsel, in responding to the motion for summary judgment below". This statement is patently untrue. This Court's attention is invited to the District Court's decision, and particularly pages A-39 and A-40, where that Court quotes from Markham's affidavit that before the option contract was executed, by him as president of In-

vestors Thrift Corporation, that contact was made with a certified public accountant, and "that a minimum of three (3) months would be required regardless of the number of personnel employed to do the work (to complete an audit of Peoples Loan & Investment Company and American Home Builders, Inc.)." Also, the District Court found it undisputed that Markham's relatives advised him to have an audit completed before closing the transaction. At page A-41, the District Court recites the undisputed fact that one of the petitioners, Vanderboom, spent several weeks in Fort Smith examining the books and records of Peoples Loan & Investment Company and American Home Builders, Inc. Certainly, petitioners considered the investigation of the companies and argued this point in the District Court. There was no denial of right or departure from the accepted and usual course of judicial procedure, and both lower Courts correctly concluded that this case should properly be determined by the accepted procedure of summary judgment.

Petitioners suggest (page 29) one investor's companion case (filed in State Court against him by respondent because of lack of jurisdictional amount) is now on appeal to the Arkansas Supreme Court, but neglects to mention the lower State Court also granted the Bank a summary judgment for the same reasons as did the Federal District Court.

Federal Court Decision in Conflict With Controlling State Law

Petitioners have suggested that both lower Courts have disregarded the statutes and decision of the State of Arkansas.

It is undisputed that petitioners borrowed substantial sums from respondent, executed notes and renewal notes, made partial payments and finally defaulted.

Although petitioners neglected to so state, it should be noted that the District Court granted respondent a summary judgment for other reasons, based upon the law of Arkansas, i. e. (1) Respondent acted in good faith in making loans to petitioners; (2) that if fraud was committed, it was on the part of the sellers of the stock and not by respondent, and that any knowledge of fraud could not be imputed to respondent; (3) petitioners waived their rights to claim fraud by extending or making payments on the notes after they alleged they had discovered fraud, and thus were estopped; and (4) the respondent, under Arkansas law, was a holder in due course of the notes sued on.

This Court has said it will not re-examine questions of local law as applied by the lower Courts. **Skelly Oil Co. v. Phillips Petroleum Co.**, 339 U. S. 667, 674 (1950).

The Court of Appeals for the Eighth Circuit once aptly said: "The competence of Judge Miller, who tried this case, to rule upon questions involving Arkansas law is not open to debate." **Mothner v. Ozark Real Estate Co.**, 300 F. 2d 617, 621 (8th Cir., 1962).

CONCLUSION

The Courts below did not create a new reasonable investor's test, nor was a new application thereof espoused. The Courts below did not generally limit the scope of protection afforded by the statutes and rules herein applicable by requiring privity between purchaser and seller, but rather held that on the facts as presented, the purchaser, Investors Thrift Corporation, was the only proper party to seek relief under the statutes and rules. The admission made by petitioners (A-21) that Investors Thrift Corporation did not receive nor act upon the alleged misrepresentations and/or concealment of material facts indicates that no valid defense has been presented. It is clearly demonstrated that the Courts below applied

the appropriate law to the uncontroverted and material facts in this cause and the decisions below are both sound on the grounds of non-imputable fraud and ratification.

Summary judgment based upon the material, basic and operative facts of the case at bar is appropriate. Both lower courts correctly determined the material facts and found no dispute, and applied the correct judicial procedure to the applicable State and Federal laws. The writ should be denied.

Respectfully submitted

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